

***United States Court of Appeals
for the Second Circuit***



**PETITION FOR
REHEARING
EN BANC**

75-5006

75-5006

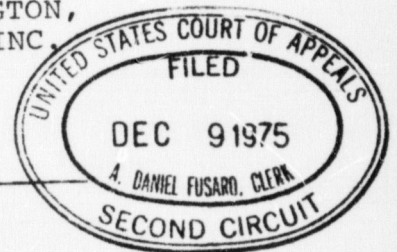
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

In the Matter

of

AMERICAN EXPRESS WAREHOUSING, LTD.,
Debtor.

PETITION FOR A REHEARING, CONTAINING A SUGGESTION
FOR A HEARING IN BANC, BY APPELLEES DUNNINGTON,
BARTHOLOW & MILLER AND SCARBURGH COMPANY, INC.



DUNNINGTON, BARTHOLOW & MILLER
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Of Counsel,

Charles L. Stewart
Steven E. Lewis

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AMERICAN EXPRESS WAREHOUSING, LTD.,

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PETITION FOR A REHEARING, CONTAINING A SUGGESTION
FOR A HEARING IN BANC, BY APPELLEES DUNNINGTON,
BARTHOLOW & MILLER AND SCARBURGH COMPANY, INC.

ISSUES

I. Should a rehearing be granted to determine whether the district court was correct in granting the application of Dunnington, Bartholow & Miller, attorneys for claimant Scarburgh Company Inc., for their fees in successfully opposing the application of the Official Creditors Committee of the Debtor for their fees in this proceeding?

II. Should a hearing in banc be ordered to determine whether the district court was correct in granting the application of Dunnington, Bartholow & Miller, attorneys for claimant Scarburgh Company, Inc., for their fees in successfully opposing the application of the Official Creditors Committee of the Debtor for their fees in this proceeding?

Statement of the Case

On March 26, 1975 Judge Sylvester J. Ryan of the United States District Court for the Southern District of New York entered an order granting the application of Dunnington, Bartholow & Miller ("Dunnington") attorneys for Scarborough Company, Inc. ("Scarborough"), for their legal fees in successfully opposing the application of the Debtor's Official Creditors Committee ("OCC") for the payment of their fees and expenses, approximately \$800,000, in this proceeding.

On April 23, 1975, the Debtor's Notice of Appeal from the Order of Judge Ryan was filed in the United States District Court for the Southern District of New York. Subsequently, on November 25, 1975, the Second Circuit, in an opinion by Chief Judge Kaufman, reversed the order of the District Court. Appellees Dunnington and Scarborough petition for a rehearing and make a suggestion for a hearing in banc.

STATEMENT OF FACTS

The debtor herein, American Express Warehousing Company, Ltd. ("Limited"), a wholly owned subsidiary of American Express Company ("Amexo"), was engaged in warehousing oils and animal fats. In 1963, Limited operated a tank farm comprised of 139 tanks leased from Allied Crude Vegetable Oil Refining Corporation ("Allied") in Bayonne, New Jersey.

Limited stored oils owned by Allied in its tanks and issued warehouse receipts to dealers, brokers and financial

institutions as security for loans made to Allied or for its account. Scarborough, as a broker, made loans to Allied, many of which were secured by receipts issued by Limited.

On November 19, 1963, Allied filed a petition in bankruptcy. The discovery of the fraudulent activities of Anthony De Angelis, Allied's president, led to investigations which disclosed that the warehouse receipts issued by Limited vastly overstated the amount of oil stated in its tanks. It soon became apparent that Limited was faced with over \$100 million of claims for missing or non-existent oils and fats.

On December 30, 1963, Limited filed for reorganization under Chapter XI of the Bankruptcy Act in the United States District Court for the Southern District of New York.

On January 28, 1964, the first meeting of Limited's creditors was held. At that meeting, the attorneys representing most of the large creditors were elected the members of the Official Creditors Committee ("OCC"). The member-attorneys of the OCC decided to retain their own firms as counsel and divide the work among themselves. They also decided to retain the services of Dewey, Ballantine, Bushby, Palmer & Wood as counsel for the OCC whose client Bunge Corporation was the only major creditor of Limited not represented by a member-attorney of the OCC.

Prior to their appointment on the OCC, these member-attorneys had reached an agreement with their clients that they would be compensated currently for their services as member-attorneys of the OCC.

Their clients and Bunge Corporation, constituting all of the largest creditors agreed among themselves to pay the OCC members-attorneys' fees on a pro rata basis, the individual ratios being the size of their claims over the total claims.

On March 8, 1974 David Hartfield, Jr., as Chairman of the OCC submitted a petition to the United States District Court, Southern District of New York, seeking an order granting an allowance for the services rendered by the member-attorneys of the OCC. The allowances, if granted, would be used to reimburse the particular creditors of Limited who paid the fees of the member-attorneys of the OCC.

Prior to submission of the petition, Dunnington informed the OCC that there was no basis in law for such an application and urged that it not be made. After the petition was filed, Dunnington informed counsel for the debtor of Dunnington's position with regard to the application and asked if they were going to oppose it. Upon being unable to persuade the OCC not to submit the petition and upon learning that the Debtor would not oppose it, Dunnington on behalf of its client, Scarburgh, submitted an affidavit and memorandum of law in opposition.

Dunnington appeared at the hearing before Judge Ryan on March 28, 1974 and argued against the OCC request. At that time, Judge Ryan ruled from the bench that he would grant the application of the OCC.

On April 26, 1974 the OCC submitted an order granting their fee application for settlement and signature. Judge Ryan, however, declined to sign the order. Subsequently, on June 6, 1974, he handed down an opinion stating that he had further studied the matter and denied the application of the OCC (Opinion No. 40787 of Judge Sylvester J. Ryan).

On January 24, 1975 Dunnington submitted an application to the United States District Court, Southern District of New York, for attorneys' fees and costs in the amount of \$39,544 incurred in Scarborough's successful opposition to the OCC petition.

In an opinion and order entered March 26, 1975, Judge Sylvester J. Ryan granted fees to Dunnington in the amount of \$26,000, which was substantially all the funds the debtor had remaining. In so doing, Judge Ryan, the judge who has directly supervised all of the proceedings in this Chapter XI proceeding for the past ten years indicated his belief that the facts giving rise to the Dunnington application satisfied the three criteria for the award of such fees laid down by this court in In re New York Investors, 130 F.2d 90, 92 (2d Cir. 1942) and In re Sapphire Steamship Lines, Inc., 509 F.2d 1242 (2d Cir. 1975).

On appeal, in an opinion written by Chief Judge Kaufman, this court reversed the district court's order granting the application of Dunnington for attorneys' fees in the amount

of \$26,000. In the Matter of American Express Warehousing, Ltd., 75-5006 (2d Cir. November 25, 1975). In so doing, the court, expressing a concern over the high cost of administering a bankrupt's estate, held that the recent decision of In re Sapphire Steamship Lines, Inc., 509 F.2d 1242 (2d Cir. 1975), barred Scarburgh from receiving its legal expenses from the debtor's estate.

Argument

POINT I

A REHEARING SHOULD BE GRANTED TO DETERMINE WHETHER THE DISTRICT COURT WAS CORRECT IN GRANTING THE APPLICATION OF DUNNINGTON, BARTHOLOW & MILLER, ATTORNEYS FOR CLAIMANT SCARBURGH COMPANY, INC., FOR THEIR LEGAL FEES IN SUCCESSFULLY OPPOSING THE APPLICATION OF THE OFFICIAL CREDITORS COMMITTEE OF THE DEBTOR FOR THEIR FEES IN THIS PROCEEDING.

1. The decision by this court reversing the order of Judge Ryan, rather than effectuating the policy of minimizing the high cost of administering a bankrupt's estate, actually will have a directly opposite impact.

In reversing the district court's order granting the application of Dunnington for fees in opposing the application of the Official Creditors Committee, this court expressed rightful concern over the high cost of administering a bankrupt's estate. In the Matter of American Express Warehousing, Ltd., 75-5006 [slip opinion] p. 2 (2d Cir. November 25, 1975).

Apparently because of this concern the court felt compelled to narrowly construe the criteria set forth in In re New York Investors, 130 F.2d 90, 92 (2d Cir. 1942), and In re Sapphire Steamship Lines, Inc., 509 F.2d 1242 (2d Cir. 1975), governing certain awards of fees of a creditor's attorney. Thus, this court concluded that three strict requirements must be met before a creditor's attorney could be awarded fees from the estate of a bankrupt: (1) the trustee or debtor in possession must have refused or neglected to act; (2) by proceeding in his stead, the creditor's counsel must have conferred a tangible benefit upon all the creditors; and (3) the attorney must have secured prior court authorization to act in place of the trustee or debtor in possession. In the Matter of American Express Warehousing, Ltd., supra, [slip opinion] at p. 2.

Assuming, that these three requirements are applicable in the instant case, petitioners respectfully submit that the decision of this court reversing Judge Ryan's order was incorrect. Rather than effectuating the policy of minimizing the high cost of administering a bankrupt's estate, the action of this court will have a directly opposite impact.

An effective way of keeping administration expenses within bounds is to have an "adversary" party monitor the administration expenses. Since the expenses of the trustees and others associated with him usually qualify as "administration expenses," and since such expenses are entitled to first prior-

ity of payment out of the general estate, 11 U.S.C. §104(a)(1), Bankruptcy Act §64(a)(1) (1970), the general creditors of the debtor are best suited for the adversary monitoring necessary for control of administration expenses. In particular, the OCC under our bankruptcy practice is the unpaid official "watchdog" representing the creditor body.

The decision by the court in this case, however, effectively terminates any creditor monitoring of excessive or unwarranted administration expenses, except for those relatively rare instances where a creditor is designated as a special counsel. Where, as in the present case, the court refuses to appoint a creditor as special counsel, In the Matter of American Express Warehousing, Ltd., supra, [slip opinion] at p. 4, it becomes economically unfeasible for a creditor to object to excessive administration expenses.

In the instant case almost all of the large creditors were represented on the OCC, and through such representation, developed a close working relationship with the debtor in possession. Under our bankruptcy practice, the OCC is designed as the unpaid official creditors' "watchdog" to make certain that the bankrupt estate is not diminished by excessive expenses of administration. Here, the OCC "watchdog" was itself seeking compensation from the estate to which it clearly was not entitled under the law. The OCC could hardly be expected to oppose its own fee application. The debtor refused to oppose it. Were it

not for Scarborough, the only effective "watchdogs" typically would be the smaller creditors with lesser amounts at stake such as Dr. Feinstein and the A. E. Staley Manufacturing Company in the instant case. The record shows that although these smaller creditors opposed the OCC fee application at the hearing, they did not brief the law to the court, nor could they be expected to do so under the circumstances. As the court refused to appoint special counsel, it is difficult to expect such creditors, with their limited resources and the smaller amounts at stake, to employ counsel for the purpose of briefing the law to the court in successfully opposing an unwarranted fee application with no hope of reimbursement for their legal expenses.

This is a far different situation from that in which general creditors are given free reign to "second guess" the Trustee responsible for administering the estate. The Second Circuit has discouraged such "second guessing" of the Trustee in his proposed settlement of claims against third parties. In re Sapphire Steamship Lines, Inc., 509 F.2d 1242, 1245 (2d Cir. 1975); In re New York Investors, 130 F.2d 90, 91-92 (2d Cir. 1942). To prevent such "second guessing" the three requirements of Sapphire were promulgated to control recovery of fees by attorneys of creditors. In cases such as the instant case, a narrow construction of these criteria would have the effect of sanctioning uncontrolled administration expense, to the detriment of the general creditors, especially ones with limited resources and smaller amounts at stake.

2. In reversing the order of Judge Ryan, the court failed to recognize the essential policy differences between Sapphire Steamship Lines, Inc., and New York Investors.

In reversing the order of Judge Ryan, the court held that the case of In re Sapphire Steamship Lines, Inc. 509 F.2d 1242 (2d Cir. 1975), barred Dunnington from receiving a fee from the debtor's estate. It is respectfully submitted by petitioners, however, that the case should be inapplicable to the present controversy on three counts, and further, that the applicable rule should be that set forth in In re New York Investors, 130 F.2d 90 (2d Cir. 1942).

Specifically, the court in Sapphire Steamship Lines, was confronted with a request for fees of a creditor's attorney for opposing a settlement of an anti-trust claim by the Trustee against a third party. This opposition ultimately led to a more generous settlement for the bankrupt estate. In denying counsel fees sought for opposing the early settlement offers, the court expressed concern that to rule otherwise would encourage creditors and their attorneys constantly to "second guess" judgments made by the Trustee charged with the estate's administration. In re Sapphire Steamship Lines, Inc., supra, at 1245. In the instant case no such "second guessing" is involved. As this court itself stated in its opinion of November 25, 1975, "it could not condone" the conduct of the OCC in making its claim for fees as an expense of administration to which it was not

entitled. Thus, the rationale for denying compensation to counsel in Sapphire Steamship Lines should not be applicable to the present case.

Secondly, the court in Sapphire Steamship Lines denied compensation for creditor opposition to a situation totally unrelated to claims for administration expenses. Consequently, disallowing a creditor's counsel fees, unless strict requirements are met, is very unlike a creditor's monitoring of administration expenses. The case of In re New York Investors, supra, specifically dealt with the issue of allowing counsel fees for opposition to claims for administration expenses. That case and its criteria should have been deemed controlling in the instant case rather than the Sapphire Steamship criteria.

Finally, the court in Sapphire Steamship Lines recognized that "special circumstances" might exist so as to waive the requirement of prior court authorization which is generally necessary for reimbursement of fees of a creditor's attorney. In re Sapphire Steamship Lines, Inc., supra, at 1246. The court in Sapphire Steamship Lines further recognized that one such special circumstance was the fact situation in New York Investors where the compensation sought was for opposing allowances for administration expenses in the form of fees for the trustee and his counsel. Since the compensation claimed by Dunnington and Scarborough in the instant case consists of the latter type of opposition, the New York Investors holding should have been

deemed controlling, and the fees claimed by petitioners should have been granted.

3. In reversing the order of Judge Ryan the court failed to recognize that Dunnington's application did satisfy the criteria laid down by the Second Circuit for the award of counsel fees.

As this court indicated, three requirements must be satisfied before a creditor's lawyer may receive fees from the debtor's estate: (1) refusal or neglect of the trustee, or debtor in possession to act; (2) achievement by the applicant of a tangible benefit for all the creditors; and (3) advance authorization by the court for the attorney to act in place of the trustee or debtor in possession. The court concluded, however, that Dunnington's application should be denied for the reason that the second and third requirements were not met. Petitioners respectfully submit that such determination was erroneous.

In particular, the court concluded that Dunnington's opposition to the OCC request did not benefit all the creditors. The court rested such a conclusion on the fact that those creditors who had contributed advances to cover the OCC's member-attorneys' fees would have recovered more individually had the OCC request been granted than they ultimately would upon receipt of their pro rata share of the estate as general creditors. Id. The problem with this reasoning is two fold, however. The requirement that all creditors benefit is a "shorthand" expression for requiring the estate, as opposed to individual creditors, to benefit by the claimant's opposition. Cf. In re New York

Investors, 130 F.2d 90 (2d Cir. 1942). The court failed to recognize the fact that the OCC application for fees as an administration expense had no legal justification. Consequently, Dunnington's opposition benefitted the debtor's estate as a whole and the creditor body pro rata, and should be sufficient to satisfy the second of the three requirements for the award of counsel fees.

The court also reversed Judge Ryan's order granting Dunnington's application for counsel fees because of Dunnington's failure to obtain formal authorization to act from Judge Ryan. In so doing, however, the court refused to apply the "special circumstances" exception as set forth in New York Investors, supra, 130 F.2d at 92, and subsequently recognized in Sapphire Steamship Lines, supra, 509 F.2d at 1246.

Specifically, the court concluded that the exception to the authorization requirement is limited to cases in which, as in New York Investors, compensation is sought for successfully opposing allowances to the trustee himself, or their counsel. As stated in New York Investors, however, this exception is based on the fact that where "the receivers, trustees or their attorneys may have personal interests so opposed to those of the creditors, only the creditors would be likely to question what was allowed." New York Investors, supra, at 92. In the instant case, in light of the close working relationship of the OCC member-attorneys and the debtor in possession, the same rationale applies.

Here the court specifically refused to appoint special counsel. In addition, the OCC, the official creditor "watchdog," was itself making the fee application as an administration expense. Thus, the "special circumstances" exception should have been applied in the instant case.

POINT II

A HEARING IN BANK SHOULD BE ORDERED TO DETERMINE WHETHER THE DISTRICT COURT WAS CORRECT IN GRANTING THE APPLICATION OF DUNNINGTON, BARTHOLOW & MILLER, ATTORNEYS FOR CLAIMANT SCARBURGH COMPANY, INC., FOR THEIR FEES IN OPPOSING THE APPLICATION OF THE OFFICIAL CREDITORS COMMITTEE OF THE DEBTOR FOR THEIR FEES AND EXPENSES IN THIS PROCEEDING.

Rule 35 of the Federal Rules of Appellate Procedure states that a hearing in banc is not favored and ordinarily will not be ordered except "(1) when consideration by the full court is necessary to secure or maintain uniformity of its decisions, or (2) when the proceeding involves a question of exceptional importance." Fed. R. App. P. 35 (a). In the instant case both conditions are present so as to favor the granting of a hearing in banc.

In particular, the court's present decision fails to apply the policy consideration of New York Investors, supra.

There is now a conflict of authority in this circuit regarding the question of when a creditor's attorney may be granted fees for successfully opposing a claim of excessive administration expenses.

Moreover, the present decision, as the court properly recognizes, involves the question of how to keep the high cost of modern bankruptcy administration under control. The instant decision will actually increase the costs of administration by eliminating creditor monitoring. In the light of the well-recognized increase in bankruptcies currently, the present proceeding involves a question of exceptional importance as set forth in Rule 35 of the Federal Rules of Appellate Procedure.

Conclusion

For the reasons set forth above, the petition for a rehearing and/or for a hearing in banc of the instant case should be granted.

Respectfully submitted,

DUNNINGTON, BARTHLOW & MILLER
Attorneys for Appellees
Dunnington, Bartholow & Miller
and Scarborough Company, Inc.

Of Counsel:
Charles L. Stewart
Steven E. Lewis

AFFIDAVIT OF SERVICE BY MAIL

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

Barbara A. Ley, being duly sworn, deposes and says that she is in the employ of Dunnington, Bartholow & Miller, attorneys for the defendant and third-party plaintiff herein, that she is over the age of eighteen years, that on the 9th day of December, 1975 she served two copies of the within "Petition for a rehearing, containing a suggestion for a hearing in banc, by Appellees Dunnington, Bartholow & Miller and Scarborough Company, Inc." upon

CADWALADER, WICKERSHAM & TAFT
Attorneys for Appellant
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Ltd., Debtor
One Wall Street
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by depositing true copies thereof securely enclosed in a post-paid wrapper in the letter box maintained and exclusively controlled by the United States Post Office Department within New York State at 161 East 42nd Street, New York, New York.

Barbara A. Ley

Sworn to before me this
9th day of December, 1975

Laure Okun

Notary Public

NOTARY PUBLIC, State of New York
No. 31-4001595
Qualified in New York County
Certificate filed in New York County
Commission Expires March 30, 1976